STATE OF IOWA
PROPERTY ASSESSMENT APPEAL BOARD

Westown Equity, LLC, Petitioner-Appellant, **v.** **Dallas County Board of Review,** Respondent-Appellee.	**ORDER** **Docket No. 11-25-0457** **Parcel No. 16-01-200-014**

On July 12, 2012, the above-captioned appeal came on for hearing before the Iowa Property Assessment Appeal Board. The hearing was conducted under Iowa Code section 441.37A(2)(a-b) and Iowa Administrative Code rules 701-71.21(1) et al. Petitioner-Appellant Westown Equity, LLC was represented by attorney Samuel I. Kreamer of Kreamer Law Firm, PC, West Des Moines, Iowa. It submitted evidence in support of its appeal. The Dallas County Board of Review designated attorney Brett Ryan of Watson & Ryan, PLC, Council Bluffs, Iowa, as its counsel. It also submitted evidence in support of its decision. The Appeal Board now having reviewed the record, heard the testimony, and being fully advised, finds:

Findings of Fact

Westown Equity, LLC, (Westown) is the owner of property located at 6000 Westown Parkway, West Des Moines, Iowa. It appeals from the Dallas County Board of Review decision reassessing its property. The real estate was classified commercial for the January 1, 2011, assessment and valued at \$14,912,930; representing \$2,811,060 in land value and \$12,101,870 in improvement value. Westown protested to the Board of Review on the ground that the property was assessed for more than authorized by law under Iowa Code section 441.37(1)(b). The Board of Review denied the protest.

Westown then appealed to this Board on the same ground. It values the property at \$9,000,000.

According to the property record card (Exhibit 2), the subject property is a general office building with 132,306[1] square feet of gross building area built in 1991. It is located at the intersection of Westown Parkway and 60th Street in the western commercial area of West Des Moines. The building is in above-normal condition with a quality construction grade of 1+05, and has 8% physical depreciation. The site improvements including 85,700 of concrete paving as well as yard lighting. It has 42% physical depreciation. The site is 9.219 acres.

Westown purchased the subject property in a lease fee transaction for $15,500,000 in April 2010 (Exhibits 22 & B). As of the January 1, 2011 assessment date, the property was fully occupied by two tenants: William Penn University and American Equity Investment Life Insurance Company (Exhibits 5 & 6). The leases are long-term and the tenants are considered good credit tenants. American Equity leases approximately 77% of the gross building area under a twelve-year, net lease. William Penn leases approximately 23% of the gross building area under a ten-year, net lease.

Thomas Knapp, a commercial appraiser, property manager, real estate broker and vice president at Ruhl & Ruhl Commercial Company, West Des Moines, testified on behalf of Westown. He testified that he brokered the sale of the subject property to a West Coast investor group that buys in the Mid-West. The group's selection criteria includes professional office properties with no vacancy or needed remodeling that are 95% to 100% occupied with better quality tenants. The subject property met the group's criteria at the time of purchase.

He stated the subject property is rated A- to B+ because of its good location. Knapp also testified the building's semi-circular front and angular rear, shape (Exhibit 14) creates some inefficiency, lacks some functionality, and costs more to remodel. Knapp reports there are 125,380 square feet of gross building area, 119,557 square-feet of rentable area and 107,950 square-feet of useable area. He describes the building as two halves connected with a three-story glass atrium.

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[1] The discrepancy in the gross building area measurements will be addressed later in this order.

Heating and cooling costs are higher because of the atrium and building shape. The building design makes office layout challenging, requires tenants to rent more space than needed, and prompts them to ask for lower rental rate. The roof and parking are twenty years old. The building has had interior updating and is in average condition for its age. Knapp comments that the 3.2/1 land to building ratio makes parking tight.

Knapp reported the former tenant vacated the building in 2008 and it was vacant until the current tenants' leases commenced. William Penn occupied the space in September 2009 and American Equity took up occupancy in December 2009. American Equity rents its portion of the building at $11 per square-foot and common area maintenance (cam) expenses. American Equity was given a $10 per square foot, or $924,000 total, tenant improvement allowance. William Penn rents its portion of the building at $10.50 per square-foot with an acceleration clause and cam expenses. William Penn was given a $50,000 moving allowance and spent approximately $821,000 to remodel the property. The tenants' uses complement each other in their need for parking space, in that, American Equity uses the parking during regular business hours and William Penn uses the parking mainly during evening hours. The property was 100% rented when Westown Equity purchased it.

Knapp testified that, in is his opinion, the purchase price reflected the leased-fee interest of the real estate, not its fee-simple value. Additionally, the quality of the tenants and the term of the leases figured into the purchase price.

Knapp prepared a stabilized operating statement using $10 market rent, 12% vacancy,[2] 7% management/leasing and 2.4% replacement reserves (Exhibit 3). Using a net operating income (NOI) of $810,029 and a 9% capitalization rate (cap rate), he estimated a $9,000,000 value for the subject property. Knapp's market rent was determined by a review of seven office leases in the immediate area (Exhibits 11(a)-11(g)). The leases are triple-net and the real estate taxes are in the cam expenses

[2] Knapp reports 20% vacancy in the subject property's competitive set, but used 12% considering more long term estimating.

paid by tenants. He provided Westown's January 1, 2011, balance sheet (Exhibit 10); 2008 through 2010 income statements (Exhibits 7-9); its property management agreement (Exhibit 12); and supporting documents for the subject property's operation (Exhibit 15-21).

In Knapp's judgment, better tenants' leases have greater value than poorer quality tenants', even with the same lease rate. As previously noted, he believes quality of the tenants and the term of the leases inflated the leased-fee sale price for the subject property above its fee-simple value. He testified that three more recent sales, which occurred three to six months after the assessment date, support this assumption.

We note that Knapp is paid on a contingency based on tax savings to Westown, thus he has a stake in the outcome of the appeal. Nevertheless, we find him knowledgeable and credible in his testimony.

In further support of its claim, Westown submitted an appraisal completed by Ted R. Frandson of Frandson & Associates, L.C. in Des Moines, Iowa (Exhibit 1). Frandson also testified at hearing. The Frandson appraisal establishes a reconciled fee simple market value for the subject property for January 1, 2011, after considering all three approaches to value: cost, sales comparison, and income. His values are as follows:

	2011 Value
Cost Approach	$12,980,000
Sales Comparison Approach	$12,540,000
Income Approach	$10,310,000
Reconciled Value	$11,500,000

Frandson describes the subject's neighborhood as being made up of offices, medical offices, and retail uses. Two new hospitals were recently built just north of the subject property on Westown Parkway, a four-lane road with turn lanes. Frandson notes the subject property has a three-story atrium in the middle of the building with granite walls and flooring, and a glass exterior. The appraisal notes reports 125,380 of gross building area, which is 6926 square feet less than the property record card.

According to the appraiser, the ground floor has a 43,010 square-foot base, and the second and third floors each have 41,185 square feet, which is less than the base measurement because of the three-story atrium.[3]

Frandson's Cost Approach

Frandson developed the cost approach to value and determined a value of $12,980,000 (rounded) for 2011 assessment year. He testified the cost approach value sets the upper limit of value. Frandson first valued the land at $3,920,000 based on four land sales, which occurred between February 2006 and March 2008. He also included one property listing. All of the sales were located in West Des Moines, Iowa. The sites ranged in size from 75,734 square feet to 294,815 square feet. The price per square foot of the sales ranged from $10.99 to $12.10. He adjusted the sales for "market conditions" or the time of sale, as well as location and size. The appraisal concludes an adjusted land value per square foot for the subject property ranging from $8.80 to $10.28. The listing was adjusted to $12.00 per square foot. Frandson reconciled to $9.75 per square foot for the land.

To value the improvements, Frandson determined the effective age of the property is 39 years, with a remaining economic life of 21 years, which resulted in total accrued physical depreciation of 65%. The effective age considers the actual age, condition, remodeling, functional utility, and location of the improvements. Frandson noted that the heating, ventilation and cooling systems (HVAC) were updated, both tenant spaces were remodeled, the roof was re-flashed in 2008 through 2009. Site improvements have estimated physical depreciation of 70%.

Frandson valued the improvements using *Marshall Valuation Service* and then applied 65% for physical depreciation, resulting in a depreciated cost of $9,059,954. Adding this figure to the land

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[3] The property record card indicates a base of 44,102 square feet and total building square feet of 132,306 (44,102 base x 3 stories). The assessment and appraisal ground floor measurements differ, and the base measurement is not adjusted for the open, atrium space between the two building wings on the second and third floors. This differences result in the discrepancy between the property record card, and the gross building area measurements used by Knapp and Frandson.

value, he estimated a total cost value of $12,980,000. Ultimately, however, Frandson's appraisal notes he gave no consideration to this approach in his final reconciliation of value.

Frandson's Sales Approach

In the sales comparison or market approach to value, Frandson first noted that limited current sale information was available. He used six sales of commercial office buildings in West Des Moines, Clive, Cedar Rapids, and Omaha, Nebraska, ranging in size from 22,305 square feet to 148,920 square feet. Frandson also included the sale of the subject property in his appraisal (Sale 1). He testified he did not adjust the sales for tenant improvement allowance or landlord concessions. We note that William Penn was given a $50,000 moving allowance and American Equity was given $924,000 in tenant improvement allowance. The sales prices ranged from $2,300,000 to $29,250,000 or $100.39 per square foot to $215.51 per square foot, and occurred between April 2004 and April 2010. Adjustments were made for market conditions, location, age/condition, quality/functional utility/finish, land-to-building ratio, and site improvements.

Frandson also adjusted two sales because they were leased-fee transactions. The appraisal notes that Sale 1 (6000 Westown Parkway, West Des Moines) and Sale 5 (1275 NW 128th Street, Clive) sold with leases in place and were adjusted downward 10% to 20% for condition of sale. Frandson testified that the leased-fee properties typically result in higher sales prices than sales of fee simple properties. To add additional support for this conclusion, Frandson also included two comparable properties that sold as leased-fees but did not include them in his adjustment grid. Frandson testified the combined effect of good rent rates, good credit tenants and good lease terms made the leased fee value of the subject property higher than its fee simple value.

Regarding his other adjustments, Frandson also testified the market was more inflated in 2006 than in 2008 when it "hit rock bottom." The older sales were adjusted downward 20% to 25% for market conditions. The indicated value ranges from $94.87 to $111.16 per square foot of gross building area. Frandson estimated market value of the subject property at $100 per square foot, for a value conclusion of $12,540,000 (rounded) by the sales approach.

Frandson's Income Approach

In the income approach to value, Frandson estimated the market rent using seven leases of office properties in West Des Moines, of which two were leases of the subject property. The leases originated in 2008 and 2009. Annual rent ranged from $8.50 to $12.12 per square foot. Estimated market rent assumed the tenant pays all expenses except management, leasing, and replacement reserves. The rates were adjusted for market condition, size, age/condition, site improvements, quality/finish/functional utility, and land/building ratio. The adjusted leases rates ranged from $8.51 per square foot to $10.45 per square foot. Based on this analysis, the estimated market rent for the subject property was $10.25 per square foot of rentable area.

Frandson reports there are several office park developments that are directly comparable to the subject office building and the market was expected to be weak in the near term given current economic conditions. Many market participants and general economic forecasts expect improvement over the next one to two years. Frandson comments that property owners have lowered their asking rental rate 10% to 20% in the last year in order to attract tenants to their buildings, are offering concessions, or using a combination of both techniques. In some instances owners are also giving rent concession of one to three months to entice tenants to sign and offering tenant improvement allowances that range from $15 to $25 per square foot. He reports there are few new tenants in the market, most of the recent transactions are existing businesses renegotiating their leases as they expire, or tenants that are moving from one location to another. The reasons for tenant relocation were for upgrading the quality of their offices, or changing the size of their offices to take advantage of the existing market that is favorable to the tenants.

Frandson also reviewed a market survey of lease listings in the West Des Moines, Clive, Des Moines and Urbandale area. He found asking rent ranged from $10 to $18 per square foot with higher rates for first floor space.

The market rates were then adjusted for vacancy and collection loss of 7% and management and leasing expense of 6%. We note Frandson used 12% vacancy rate in his analysis and the survey for the western suburban area for class A office space estimated a 21% vacancy rate (Exhibit 1-page 90). Adjustments were also made for collection loss, management fees, leasing fee, and replacement reserves to determine a net operating income (NOI) of $979,130.

Frandson then determined a cap rate to apply to the NOI. He extracted a cap rate from six office buildings in the Des Moines Metro area, including three from the leased-fee transactions and the subject properties' two leases. The cap rates from local sales ranged from 7.88% to 8.41%. We note only one sale property had a stabilized NOI. He then determined a 10.61% cap rate using a mortgage equity analysis. Frandson reconciled to a 9.50% overall capitalization rate. In his opinion, the greater risk to investors justifies a higher cap rate when developing the sale approach from fee-simple sales.

Using this rate, the subject property's estimated value is $10,310,000 (rounded) by the income approach.

In determining a reconciled value for the subject property, Frandson considered the sales approach but commented that most of the sales either are older transactions requiring estimated market conditions adjustments or are leased-fee transaction also requiring adjustments. He gave more consideration to the income approach because it included current market information. He explained that the income approach was the most conclusive because current market rents were used. Frandson testified he gave no weight to the cost approach. Frandson concluded a final reconciled value of $11,500,000 as of January 1, 2011.

Rich Hughes testified on behalf of the Board of Review. He testified retired from private sector work where he conducted market studies and reviewed appraisals. In his opinion, the difference in value between a fee-simple sale and a leased-fee sale can be measured by the guaranteed income stream inherent in a leased-fee transaction. No exhibits were presented to show his calculations, but he testified he believed the leased-fee sale of the subject property was valued approximately $500,000 more than if it had been a fee-simple transaction.

Only when questioned about his involvement in the assessment of the subject property, did Hughes reveal that he has worked for the Dallas County Assessor's office for two years and, in fact, was involved in the subject property's assessment during that period. He indicated the 2009 assessments reflected a 40% vacancy factor he put on the property. In his review for the 2010 assessment, he removed the vacancy factor, then adjusted the property by a 20% functional obsolescence factor to adjust for the classroom finish. We note the property record card notations shows a 20% adjustment made by RH; however, it was not applied in the cost report.

We note that if the 20% functional obsolescence factor had been applied to the 2010/2011 revaluation, as intended by Hughes, the assessment in dispute would be reduced by nearly $3,000,000. Thus, the 2011 assessed value would be roughly $12,000,000, and would reconcile with Frandson's value of $11,500,000.

Hughes appeared to be acting deceitful by not testifying on direct examination that he was involved with the assessment of the subject property. Additionally, his testimony lacked credibility because he had no additional evidence to support his calculations. We, therefore, give it no weight.

The Board of Review argues that the sale price of the subject property should definitively determine its fair market value and assessment. While the sale price of the subject property should be considered in arriving at market value; it is not alone conclusive. If there are sale factors that distort the purchase price, it must be adjusted to remove the distorting influence. Ample evidence was presented to show the sale price of the subject property was inflated due to the leased-fee sale condition. Additionally, the assessment is unreliable because it was based on incorrect measurements and the functional obsolescence adjustment was not applied.

We find Frandson to be qualified, experienced, and knowledgeable appraiser. We find his appraisal to be the best evidence of the fair market value of the subject property and it supports Westown's claim of over-assessment as of January 1, 2011.

Conclusions of Law

The Appeal Board based its decision on the following law.

The Appeal Board has jurisdiction of this matter under Iowa Code sections 421.1A and 441.37A (2009). This Board is an agency and the provisions of the Administrative Procedure Act apply to it. Iowa Code § 17A.2(1). This appeal is a contested case. § 441.37A(1)(b). The Appeal Board determines anew all questions arising before the Board of Review related to the liability of the property to assessment or the assessed amount. § 441.37A(3)(a). The Appeal Board considers only those grounds presented to or considered by the Board of Review. § 441.37A(1)(b). But new or additional evidence may be introduced. *Id.* The Appeal Board considers the record as a whole and all of the evidence regardless of who introduced it. § 441.37A(3)(a); *see also Hy-vee, Inc. v. Employment Appeal Bd.*, 710 N.W.2d 1, 3 (Iowa 2005). There is no presumption that the assessed value is correct. § 441.37A(3)(a).

Property is to be valued at one hundred percent of its actual value. § 441.21(1)(a). Actual value is the property's fair and reasonable market value. *Id.* "Market value" essentially is defined as the value established in an arm's-length sale of the property. § 441.21(1)(b). Sales prices of the property or comparable properties in normal transactions are to be considered in arriving at market value. *Id.* If sales are not available or market value "cannot be readily established in that manner," "other factors" may be considered in arriving at market value. *Heritage Cablevision v. Board of Review of City of Mason City,* 457 N.W.2d 594, 597 (Iowa 1990); Iowa Code § 441.21(2). "To determine whether other properties are sufficiently comparable to be used as a basis for ascertaining market value under the comparable-sales approach, [the Supreme Court] has adopted the rule that the conditions with respect to the other land must be 'similar' to the property being assessed." *Soifer v. Floyd County Bd. of Review*, 759 N.W.2d 775, 783 (Iowa 2009). "Similar does not mean identical, but having a resemblance; and property may be similar . . . though each possess various points of difference." *Id.* Determining comparability of properties is left to the "sound discretion" of the trier of fact. *Id.* Consideration should be given to size, use, location, and character, as well as the nature and timing of the sale. *Id.* This Board is "free to give no weight to proffered evidence of comparable sales which it finds not to be reflective of market value." *Heritage Cablevision*, 457 N.W.2d at 598.

The property owner bears the burden to prove that an assessment is excessive. If the property owner "offers competent evidence by at least two disinterested witnesses that the market value of the property is less than the market value determined by the assessor," the burden shifts to the Board of Review. Iowa Code § 441.21(3). A disinterested witness is defined as, "[o]ne who has no right, claim, title, or legal share in the cause or matter in issue, and who is lawfully competent to testify." *Post-Newsweek Cable, Inc. v. Bd. of Review of Woodbury County*, 497 N.W.2d 810, 813 (Iowa 1993). In this case, although Westown introduced testimony of two witnesses, and under the statutory definition Knapp appears to be a disinterested witness, because he gave no testimony regarding the market approach to valuation, his testimony would not be "competent" to *shift the burden. Soifer*, 759 N.W.2d at 780. Nevertheless, failing to shift the burden does not mean Westown cannot succeed in the appeal. *Id.*

In an appeal that alleges the property is assessed for more than the value authorized by law under Iowa Code section 441.37(1)(b), there must be evidence that the assessment is excessive and the correct value of the property. *Boekeloo v. Bd. of Review of the City of Clinton*, 529 N.W.2d 275, 277 (Iowa 1995).

Despite the Board of Review's assertion to the contrary, we think it is clear from the wording of section 441.21(1)(b) that a sales price for the subject property in a normal transaction is a matter to be considered in arriving at market value but does not *conclusively* establish that value. *Riley v. Iowa City Board of Review*, 549 N.W.2d 289, 290 (Iowa 1996) (holding the same).

Furthermore, a sales price in an abnormal transaction is not to be taken into account unless the distorting factors can be clearly accounted for. Iowa Code § 441.21(1)(b). In this case, a leased-fee transaction is not the same as fee-simple transaction. The proper measure of the value of commercial property is what the property would bring if sold in fee simple, free and clear of any leases. *I.C.M. Realty v. Woodward*, 433 N.W.2d 760, 762 (Iowa Ct. App. 1988). The evidence shows that a leased-fee sale, particularly one with favorable lease terms and good tenants, tends to distort the purchase price upward. The Board of Review's claim that the leased-fee sales price should be the assessment is also contradictory if applied to a situation where the property sold at a discount because of unfavorable leases. *See Merle Hay Mall v. City of Des Moines Board of Review*, 564 N.W.2d 419 (Iowa 1997). In that case, it would have been inequitable to reduce the Mall's assessment because of its "poor business acumen." *Id.* at 422. We are convinced that Westown paid a premium for the quality tenants and long-term lease. And "[w]hile rental income which might be received from a particular lease is *some* evidence its value, such evidence may only be considered in determining what that value would be, *independent of the lease*." *Oberstein v. Adair County Bd. Of Review*, 318 N.W.2d 817, 821 (Iowa App. 1982) (emphasis added). The leased-fee, sale price of the subject property was not reflective of the property's fee-simple market value; and it is not the value section 441.21(1)(b) is attempting to capture for assessment purposes. Therefore, it alone is not the proper measure of fair market value for assessment purposes.

The best evidence in the record, Frandson's fee-simple appraisal, shows the subject property is over assessed. Viewing the record as a whole, we determine that the Frandson appraisal, and the preponderance of the evidence supports, Westown's claim of over-assessment. Therefore, we modify the Westown's property assessment.

THE APPEAL BOARD ORDERS that the January 1, 2011, assessment of the Westown Equity's property located in West Des Moines, Iowa, as determined by the Dallas County Board of Review, is modified to $11,500,000.

The Secretary of the State of Iowa Property Assessment appeal Board shall mail a copy of this Order to the Dallas County Auditor and all tax records, assessment books and other records pertaining to the assessment referenced herein on the subject parcel shall be corrected accordingly.

Dated this 14 day of September 2012.

Jacqueline Rypma

Jacqueline Rypma, Presiding Officer

Richard Stradley, Board Chair

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Certificate of Service
The undersigned certifies that the foregoing instrument was served upon all parties to the above cause & to each of the attorney(s) of record herein at their respective addresses disclosed on the pleadings on 9-14, 2012
By: ✓ U.S. Mail ___ FAX
___ Hand Delivered ___ Overnight Courier
___ Certified Mail ___ Other
Signature